

Office of Chief Counsel
Internal Revenue Service

memorandum

CC:SB:1:MAN:TL-N-910-01
LABranche

date:

to: Chief of Appeals, Manhattan
Attn: Leslie Kaplan, Appeals Officer

from: Area Counsel, Manhattan

subject: [REDACTED] Donor
SS: [REDACTED]

Review of Statutory Notice of Deficiency

Statute of limitations expires: [REDACTED]

DISCLOSURE STATEMENT

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Pursuant to your request of February 6, 2001, we have reviewed the notice of deficiency which you propose to issue to the above-named taxpayer. After careful review of the administrative file, we concur with the issuance of the proposed notice of deficiency at this time based on the information developed. However, we recommend that, in addition to the valuation position, an alternative position be taken which

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characterizes the transfer of stock to the family limited partnership as an indirect gift of stock by the donor to the trust and/or his children. Our recommendation is based on the analysis below.

Property transferred for less than adequate consideration is generally deemed a gift. See I.R.C § 2512(b). A gift may be direct or indirect whether the transfer is in trust or otherwise. See Treas. Reg. 25.2511-1(a). The gift is measured by the value of the property in the hands of the donor rather than by the value of the property received by the donee. See Treas. Reg. 25.2511-2(a). An example of an indirect transfer is provided by Treas. Reg. 25.2511-1(h)(1) which states that a transfer of property by an individual to a corporation for less than full consideration represents gifts by the individual to other shareholders of the corporation to the extent of their proportionate interest. Moreover, a transfer to a partnership for less than full consideration may represent an indirect gift to the partners. See Gross v. Commissioner, 7 T.C. 873 (1946).

In the instant case, the [REDACTED] Limited Partnership was formed on [REDACTED]. On that same date the [REDACTED] Trust was established. [REDACTED] was the general partner with a [REDACTED]% interest in the partnership and the [REDACTED] Trust held a [REDACTED]% ownership. On [REDACTED] [REDACTED] gifted a [REDACTED]% partnership interest to the [REDACTED] Trust, designating [REDACTED] as a gift for the benefit of each of his [REDACTED] children. Simultaneously, he transferred [REDACTED] shares of stock to the [REDACTED] Limited Partnership. The partnership agreement at [REDACTED] provides that, "any partner ... who shall acquire an interest ... by means of a transfer ... shall have a capital account which reflects such transfer." Therefore, [REDACTED] made a transfer for less than adequate value in that his capital account did not reflect the contribution he made. Consequently, this was an indirect gift of stock to the [REDACTED] Trust and/or the donees.

The facts in this case are similar to the facts in Shepherd v. Commissioner, 2000 U.S. Tax Ct. LEXIS 77, 115 T.C. No. 30 (Oct. 26, 2000). In Shepherd a family limited partnership was formed on August 2, 1991, with J.C. Shepherd (father) having a 50% ownership interest and each of his two sons a 25% ownership interest. J.C. Shepherd then transferred leased property to the partnership on the same day the partnership came into existence, and one month later, transferred stock to the partnership. The court concluded that both transfers of leased property and stock were indirect gifts to each of his sons because the contributions were allocated to the sons' capital accounts based on their

respective partnership shares. Because the contributions were reflected partially in the capital accounts of the noncontributing partners, the values of the noncontributing partners' interests were enhanced by the contributions of the taxpayer. Moreover, upon dissolution, each partner was entitled to receive payment of the balance of his capital account.

In light of the analysis above, we suggest that you insert the following language in the Explanation of Adjustments as additional explanations to Items 1-3.

"In the alternative, it is determined that the transfer of the [REDACTED] stock to the [REDACTED] Limited Partnership is in substance an indirect gift within the meaning of IRC § 2511 of [REDACTED] percent of that stock to the other partners.

In the alternative, It is determined that the fair market value of two [REDACTED] percent interests and a [REDACTED] percent interest in the [REDACTED] FLP is \$[REDACTED]."

The 3615-A uses [REDACTED] as the amount of the gifts, but the gifts only add up to [REDACTED]. Please reconcile this difference.

Item 1 of the Explanation of Adjustments should begin with "It is determined". In addition, in Items 1-3 "value" should be "fair market value." Also, the "\$" is missing from Item 1 of Schedule A, Part 1.

Please verify the correct address of [REDACTED]. Although the [REDACTED] shows the address to be c/o [REDACTED] that lawfirm has been out of business for a few years.

If you have further questions concerning this matter, please contact attorney Lydia Branche at (212) 264-5473.

LINDA R. DETTERY
Area Counsel, SBSE

By: _____
LYDIA A. BRANCHE
Attorney

Enclosure: Administrative file.